



South African Reserve Bank

Media Statement

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Changes to the money-market liquidity management strategy of the South African Reserve Bank

The South African Reserve Bank (SARB) reviews its monetary-policy implementation framework on a continuous basis and refinements are effected when deemed necessary. The key objective of the current repo-based accommodation system is to use active liquidity management through discretionary market operations as the main operational tool for monetary policy implementation.

The SARB currently employs a classical cash reserve or liquidity deficit framework for the implementation of monetary policy, with the repo rate as the operational variable. The theoretical underpinning of this system is that the central bank creates a shortage of liquidity in the money market (known as a money-market shortage) in order to ensure that banks have a measure of dependency on the central bank for the refinancing of their liquidity requirements. Within this system, the size of the money-market shortage is, therefore, of critical importance.

The principle is that the money-market shortage should be equal to the total of the banks' required cash reserve balances with the SARB. This is perceived to be the level at which the dynamics of the cost of funding of banks and the additional liquid financial assets held as collateral for the refinancing of the money-market shortage would be optimal to allow for an effective monetary policy transmission mechanism. While the transmission mechanism of monetary policy is working, too low a level of the shortage risks making it vulnerable at times.

The decline over time in the money-market shortage as a percentage of commercial bank assets, as well as its ratio to notes and coin in circulation outside the SARB, have presented operational challenges as the short-term seasonal fluctuations in note flows have occasionally been close to the level of the money-market shortage. To further improve the effectiveness of the monetary-policy implementation framework and to enhance the SARB's control of money-market liquidity and short-term money-market rates, the SARB deems it necessary to increase the level of the money-market shortage to a more appropriate level over time. Going forward, the trend growth in the money-market shortage will reflect developments in the notes and coin in circulation outside the SARB as well as in the banks' required cash reserve balances with the central bank.

Any changes to the liquidity management strategy by the SARB should not be construed to be providing any signals with regard to the future monetary policy stance.

The SARB has embarked on a process of engagement with market participants through the Financial Markets Liaison Committee.

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